

Consultation Response

AFME response to PRA LIAC01/26

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The Association for Financial Markets in Europe (AFME) welcomes the opportunity to comment on the Prudential Regulation Authority's (PRA) Low Impact Amendments Consultation LIAC01/26. AFME is the voice of the leading banks in Europe's financial markets, providing expertise across a broad range of regulatory and capital markets issues. We represent over 150 leading global and European banks and other significant market players. Our members play a vital role in Europe's financial ecosystem, underwriting around 90% of European corporate and sovereign debt, and 85% of European listed equity capital issuances. Importantly, AFME members are market makers, providing liquidity, which is essential for ensuring financial markets can function efficiently. We also represent law firms and other associate members which advise market participants and support AFME's legal and regulatory initiatives.

Introduction

AFME and its members have identified a small number of important points requiring review before the amendments set out in LIAC01/26 are finalised. These are set out below. We remain available to discuss our submission.

Amendments to the Groups Part of the PRA Rulebook

The inclusion of the reference to voting rights means it is now unclear whether voting rights or share of capital should take precedence in cases where there are different percentages of share capital and voting rights, when applying proportional consolidation. We encourage the PRA to clarify whether the intention is that it is the higher percentage which should take precedence. This clarification will be helpful as there are two stages to the process: determining if a Participation exists and then actual proportional consolidation.

We also encourage the PRA to clarify that once an investment is classified as 'Participation' or 'Capital Ties', then the "Proportional Consolidation Calculations" should be performed based on capital held only and not voting rights, in line with the applicable accounting treatment.

Voting rights being the determinant of the percentage of proportional consolidation will be more relevant for a 'company limited by guarantee'. In case of 'company limited by shares', we would appreciate more clarity. If actual proportional consolidation is done based on voting rights instead of capital, this would be a departure from accounting standards.

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Amendments to the Countercyclical Capital Buffer Rates UK Technical Standard

We are concerned that the proposed amendments to the definition of ‘trading book exposure’ in the UK Technical Standard on the identification of the geographical location of the relevant credit exposures for calculating institution-specific countercyclical buffer rates introduce a significant lack of clarity and narrow the definition.

Specifically, the proposed amendments only refer to the Simplified Standardised Approach. However, many firms will not apply the Simplified Standardised Approach. The drafting risks being interpreted as suggesting that firms that do not apply the Simplified Standardised Approach do not have trading book exposures for the purpose of the Regulation, which we believe does not align with the PRA’s intention.

The proposed amendments to the definition of ‘trading book exposure’ also appear to conflict with rule 3.1 (3) in the PRA Rulebook chapter on the Countercyclical Capital Buffer, which says:

“For the purposes of (2), a *firm* must calculate its total *own funds* requirements for credit risk, default risk, specific risk, incremental default and migration risk in accordance with Part Three, Title II of CRR, the Market Risk: Simplified Standardised Approach (CRR) Part, Market Risk: Advanced Standardised Approach (CRR) Part and Market Risk: Internal Model Approach (CRR) Part.”

In addition, for firms that apply the Advanced Standardised Approach for example, the drafting proposed in LIAC01/26 would lead to a disconnect as firms would need to calculate the own funds inputs for the Countercyclical Capital Buffer under the Simplified Standardised Approach following Articles 326 to 350, whereas a firm’s own funds requirement for default risk would be calculated under the Advanced Standardised Approach articles (Section 5 Articles 325v to 325ad).

We recommend that the definition of ‘trading book exposure’ in the Technical Standard be reviewed and amended to ensure it is clear, achieves the intended effect, and is not unnecessarily narrowed. We would be happy to discuss possible wording with the PRA.

Finally, we note the references in Article 3(2) of the Technical Standard to the Market Risk: Internal Model Approach (CRR) Part of the PRA Rulebook. The wording suggests that this is a reference maintained for the current Internal Model Approach rules with respect to the requirements for the incremental default and migration risk, reflecting that FRTB-IMA will only apply from January 2028. We would welcome confirmation from the PRA that this is correct, that Article 3 will be removed subsequently, and that the wording in the PRA Rulebook on Capital Buffers will also be subsequently amended to remove reference to “incremental default and migration risk” once the transitional period for the current Internal Model Approach has expired (in addition to reviewing the definition of trading book exposure subject to the amendments to the definition which are made by the PRA).